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TAGS: EINV EIND ETRD SF
SUBJECT: The South African Motor Industry

¶1. (U) Summary: In 1995, the Department of Trade and Industry (DTI) introduced the South African Motor Industry Development Program (MIDP) to promote production and exports of locally produced vehicles. The DTI recently announced that between 2005-2006 it would review the MIDP as part of a long-term strategy aimed at the continued growth of the industry. Since introduction of the MIDP, industry exports have grown at an annual rate of 33%, South Africa has become known as a high-quality niche producer, and a number of international companies have expanded or located production plants here. Nevertheless, South Africa remains a fringe player in global markets. Exports account for just 0.20% of global demand, and domestic demand accounts for only 0.70% of global production. South Africa wants to increase its share of global production so as to become a global player. In December 2002, the government extended the MIDP to 2012, but there are doubts about whether it can or should retain its current form until then. End Summary.

The Motor Industry Development Program

¶2. (U) In 1995, the Department of Trade and Industry introduced the MIDP to rejuvenate the industry by promoting the local manufacture and export of vehicles. At the heart of the MIDP is an import-export formula that rewards exports with import duty credits. Companies get a rebate on import tariffs equal to 100% of the local content value of their exports. This is supposed to be phased down to 70% in 2009. Meanwhile, protective import tariffs are supposed to be phased down from 40% to 30% in 2007, and 25% in 2012 (completely knocked down components from 30% to 25% in 2007, and 20% in 2012). Trade rivals describe the MIDP as an export incentive, and question whether it contravenes World Trade Organization rules. Australia, whose own motor industry strategy was partly the model for the MIDP, has been one of the strongest critics. South African and Australian officials have held several rounds of discussions on the MIDP. Following the round held in Canberra on August 27, 2004, both sides agreed to cooperate during the upcoming review of the MIDP. Australia will share its experience.

¶3. (U) Prior to the initiation of the MIDP, South Africa's motor manufacturing industry was in the doldrums. Vehicle exports numbered only 15,760 units, or 4% of local production. From 1996 to 2002, under the MIDP, exports grew at an average of 33% a year. In 2002, they represented 31% of total production. Exports have since leveled off at about 125,000 annual units because of the strength of the rand. The National Association of Automobile Manufacturers of South Africa (NAAMSA) expects export growth to resume its 30% growth trajectory in 2005.

The Motor Industry

¶4. (U) The South African motor industry comprises manufacturers of whole vehicles as well as parts, plus retailers and after-sale maintenance service providers. Of nineteen major companies, eight are larger manufacturers that produce light and heavy vehicles, and eight are smaller specialist manufacturers that produce commercial/heavy vehicles and components.

¶5. (U) In 2003, total local vehicle production was 421,300 units, and imports were 87,900 units. Exports totaled 126,000 units (not including sales to the SACU countries), consisting of 114,900 cars and 12,000 light and heavy commercial vehicles, and account for 0.2% of global demand. NAAMSA projects 2004 domestic demand to increase by 13%, and Tony Twine, an independent industry analyst from Econometrix, thinks that total vehicle production could reach a 20-year high of 465,000 units for 2004, and grow by a further 13% in 2005.

¶6. (U) The industry is important to South Africa as a revenue generator, foreign exchange earner, investor, and employer. On the strength of exports, the industry has increased its contribution to GDP from 4.9% in 1999 to 6.6% in 2003. In 2003, the industry invested $350 million in the economy. It earned $22 billion in income from domestic activities, $3 billion from built-up vehicle exports, and $3.5 billion from component exports. Fuel industry income (net of taxes) added another $14 billion. Employment in the industry exceeded 300,000, with the manufacturing and retail sectors employing

112,000 and 194,000, respectively.

Niche Player

¶7. (U) According to Twine, speaking to a breakfast meeting in Johannesburg on September 9, the South African motor industry is not a mass producer of vehicles or components. Rather, it is a competitive niche producer of certain vehicle models and specialized components. There is growing international reliance on South Africa to produce cars and commercial vehicles for right-hand-drive countries, engines and components for specific cars such as the VW Golf, and specific models such as the BMW 300 series and the C-class Mercedes Benz for export.

¶8. (U) Twine said that he did not believe that the South African motor industry could establish a "home-grown" industry. There was too much global competition and excess capacity for such a strategy to succeed. However, he felt that South Africa was on the way to becoming a more important niche player. Future success depended on the ability of local industry to navigate a competitive course by capitalizing on new niche markets (such as hybrid vehicles) and new technology (such as fuel cells), which offered opportunities for growth through innovation. Twine reckoned that South Africa would have to produce over 2 million vehicles annually (roughly 4% of world production) to become a global player -- even as a niche producer. He estimated that South Africa was more than 10% of the way to reaching this goal.

South Africa as an Investment Location

¶9. (U) Twine believes that international motor companies were attracted to South Africa for a number of reasons: 1) South Africa's relatively advanced economy and infrastructure were conducive to supporting a sophisticated, mature industry; 2) the availability of a sufficiently skilled work force; 3) an existing local supply and support services industry 4) a comparative advantage in raw material supply; 5) an emerging market and the potential to grow with the black middle class in South Africa and elsewhere in sub-Saharan Africa. He noted that while the black middle class market-share had increased to 31% in South Africa, other sub-Saharan markets had not yet materialized. Currently, the Southern African Customs Union (SACU) countries (which include South Africa, Botswana, Namibia, Lesotho, and Swaziland) account for more than 70% of the sub-Saharan market.

¶10. (U) On potential threats to the South African motor industry, Twine thought that an economic slow-down in either India or China would cause companies there to export excess production to places like South Africa, where production costs were twice as high. He pointed out that although local industry was partially integrated into global manufacturing networks, it was still a minor player, with most decisions made in boardrooms overseas. This meant that South Africa was especially vulnerable to a variety of external events.

¶11. (U) Twine cited possible government intervention in the areas of Black Economic Empowerment (BEE) and pricing as a risk factor for the industry that would negatively affect foreign investors. For example, if BEE policies were to require foreign-owned firms to sell equity to local BEE partners, those local partners might have difficulty ponying up $30-50 million for model retooling every five to seven years. This could mean that foreign auto manufacturers might have to constantly search for new BEE investors to maintain a minimum BEE share ratio. To date, however, there is no BEE charter for the motor industry, but it is in the works. Another sensitive point would be if parent companies had to share the profits with their new BEE partners, even after having incurred most of the investment risks up front. Twine also noted labor hostility to the industry as a negative factor, based as it is on union misperception that the South African auto industry is vital to multinational parent companies.

¶12. (U) DTI Director of BEE Partnerships Jeffrey Ndumo has indicated that auto manufacturers will have latitude in pursuing either enterprise charters or a sectoral charter. DTI does not have a preference of either way. Ndumo said that if the auto manufactures pursue a sectoral charter, DTI is encouraging them to frame it as a set of broad guidelines that would include the components market as well. Ndumo said DTI was sensitive to the issue of selling equity for auto manufactures and was encouraging them to find a "creative" solution to satisfy equity requirements.

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